

(2) The election shall be made for each mine or other natural deposit by a clear indication on the return or by a statement filed with the district director with whom the return was filed, not later than the time prescribed by law for filing such return (including extensions thereof) for the taxable year to which such election is applicable.

(c) *Expenditures made by the owner who retains a non-operating mineral interest.* (1) A taxpayer who elects to defer exploration expenditures and thereafter transfers his interest in the mine or other natural deposit, retaining an economic interest therein, shall deduct an amount attributable to such interest on a pro rata basis as the interest pays out. For example, a taxpayer who defers exploration expenditures and then leases his deposit, retaining a royalty interest therein, shall deduct the deferred expenditures ratably as he receives royalties. If the taxpayer receives a bonus or advanced royalties in connection with the transfer of his interest, he shall deduct deferred expenditures allocable to such bonus or advanced royalties in an amount which is in the same proportion to the total of such costs as the bonus or advanced royalties bears to the bonus and total royalties expected to be received. Also, in the case of a transfer of a mine or other natural deposit by a taxpayer who retains a production payment therein, he shall deduct the exploration expenditures ratably over the payments expected to be received.

(2) Where a taxpayer receives an amount, in addition to retaining an economic interest, which amount is treated as from the sale or exchange of a capital asset or property treated under section 1231 (except coal or iron ore to which section 631(c) applies), the deferred exploration expenditures shall be allocated between the interest sold and the interest retained in proportion to the fair market values of each interest as of the date of sale. The amount allocated to the interest sold may not be deducted, but shall be a part of the basis of such interest.

(d) *Losses from abandonment.* Section 165 and the regulations thereunder contain general rules relating to the treat-

ment of losses resulting from abandonment.

(e) *Computation of amount of deduction.* The amount of the deduction allowable during the taxable year is an amount A, which bears the same ratio to B (the total deferred exploration expenditures for a particular mine or other natural deposit reduced by the amount of such expenditures deducted in prior taxable years) as C (the number of units of the ore or mineral benefited by such expenditures sold during the taxable year) bears to D (the number of units of ore or mineral benefited by such expenditures remaining as of the taxable year). For the purposes of this proportion, the *number of units of ore or mineral benefited by such expenditures remaining as of the taxable year* is the number of units of ore or mineral benefited by the deferred exploration expenditures remaining at the end of the year to be recovered from the mine or other natural deposit (including units benefited by such expenditures recovered but not sold) plus the number of units benefited by such expenditures sold within the taxable year. The principles outlined in § 1.611-2 are applicable in estimating the number of units remaining as of the taxable year and the number of units sold during the taxable year. The estimate is subject to revision in accordance with that section in the event it is ascertained from any source, such as operations or development work, that the remaining units are materially greater or less than the number of units remaining from a prior estimate.

[T.D. 6500, 25 FR 11737, Nov. 26, 1960, as amended by T.D. 6685, 28 FR 11405, Oct. 24, 1963; T.D. 6841, 30 FR 9306, July 27, 1965; T.D. 7192, 37 FR 12939, June 30, 1972]

§ 1.615-4 Limitation of amount deductible.

(a) *Taxable years beginning before July 7, 1960.* For any taxable year beginning before July 7, 1960 (including taxable years of less than 12 months), a taxpayer may deduct or defer exploration expenditures paid or incurred in the taxable year in an amount not in excess of \$100,000. However, for such taxable years, the taxpayer may not avail himself of the provisions of section 615

for more than four taxable years (including taxable years of less than 12 months and taxable years subject to the Internal Revenue Code of 1939). Such four taxable years need not be consecutive. In determining the number of years in which a taxpayer has availed himself of section 615, a year for which he makes an election to defer exploration expenditures shall count as one year. Any subsequent taxable year in which such deferred expenditures are deducted shall not be taken into account as one of the four years. For purposes of the 4-year limitation, a year in which both a deduction and an election to defer are availed of by the taxpayer shall be taken into account as only one year.

(b) *Taxable years beginning after July 6, 1960.* For any taxable year beginning after July 6, 1960 (including taxable years of less than 12 months), a taxpayer who is otherwise eligible may deduct or defer exploration expenditures paid or incurred before January 1, 1970, in the lesser of the following amounts:

(1) The amount paid or incurred in the taxable year,

(2) \$100,000, or

(3) \$400,000 minus all amounts deducted or deferred for taxable years ending after December 31, 1950.

For purposes of this paragraph, the number of taxable years for which the taxpayer availed himself of the provisions of section 615 or the corresponding provisions of prior law is immaterial.

(c) *Special rules for previously deferred expenditures.* In determining whether an election to defer was availed of in applying the limitations of paragraphs (a) and (b) of this section, there shall be taken into account any year with respect to which amounts were deferred but not fully deducted because of a sale or other disposition of the mineral property, even though the balance of the deferred amounts was treated as part of the basis of the mineral property in determining gain or loss from the sale.

(d) *Example of application of provisions.* The application of the provisions of subparagraphs (a) and (b) of this section may be illustrated by the following example:

Example. A taxpayer on the calendar year basis, who has never claimed the benefits of section 615, or section 23(ff) of the 1939 Code, expended \$200,000 for exploration expenditures during the year 1956. For each of the years 1957, 1958, 1959, and 1960 the taxpayer had exploration costs of \$80,000. The taxpayer deducted or deferred the maximum amounts allowed for each of the years 1956, 1957, 1958, and 1959. None of the \$80,000 expenditures for 1960 could be deducted or deferred by the taxpayer because he had already deducted or deferred exploration expenditures for 4 prior years. In 1961 the taxpayer expended \$200,000 for exploration expenditures. The maximum amount the taxpayer may deduct or defer for the taxable year 1961 is \$60,000 computed as follows:

(1) Add all yearly amounts deducted or deferred for exploration expenditures by the taxpayer for prior years.

| Year | Expenditures | Deducted or deferred |
|-------------|--------------|----------------------|
| 1956 | \$200,000 | \$100,000 |
| 1957 | 80,000 | 80,000 |
| 1958 | 80,000 | 80,000 |
| 1959 | 80,000 | 80,000 |
| 1960 | 80,000 | 0 |
| Total | | 340,000 |

(2) Subtract the sum of the amounts obtained in (1), \$340,000, from \$400,000, the maximum amount allowable to the taxpayer for deductions or deferrals of exploration expenditures.

| | |
|--|--------------|
| Maximum amount allowable to taxpayer | \$400,000 |
| Sum of amounts obtained in (1) | 340,000 |
| | <hr/> 60,000 |

(e) *Transferee of mineral property.* (1) Where an individual or corporation transfers any property to the taxpayer and the transfer is one to which any of the subdivisions of this subparagraph apply, the taxpayer shall take into account for purposes of the 4-year limitation described in paragraph (a) of this section, all years that the transferor deducted or deferred exploration expenditures, and for purposes of the \$400,000 limitation described in paragraph (b) of this section, all amounts that the transferor deducted or deferred.

(i) The taxpayer acquired any mineral property in a transaction described in section 23(ff)(3) of the Internal Revenue Code of 1939, excluding the reference therein to section 113(a)(13).

(ii) The taxpayer would be entitled under section 381(c)(10) to deduct exploration expenditures if the transferor (or distributor) corporation had elected to defer such expenditures. For example, if the taxpayer acquired any mineral property in a transaction described in section 381(a) (relating to the acquisition of assets through certain corporate liquidations and reorganizations), there shall be taken into account in applying the limitations of paragraph (a) of this section the years in which the transferor exercised the election to defer or deduct exploration expenditures, and there shall be taken into account in applying the limitations of paragraph (b) of this section any amount so deducted or deferred. See also section 381(c)(10) and the regulations thereunder.

(iii) The taxpayer acquired any mineral property under circumstances which make applicable the following sections of the Internal Revenue Code:

(a) Section 334(b)(1), relating to the liquidation of a subsidiary where the basis of the property in the hands of the distributee is the same as it would be in the hands of the transferor.

(b) Section 362 (a) and (b), relating to property acquired by a corporation as paid-in surplus or as a contribution to capital, or in connection with a transaction to which section 351 applies.

(c) Section 372(a), relating to reorganization in certain receiverships and bankruptcy proceedings.

(d) Section 373(b)(1), relating to property of a railroad corporation acquired in certain bankruptcy or receivership proceedings.

(e) Section 1051, relating to property acquired by a corporation that is a member of an affiliated group.

(f) Section 1082, relating to property acquired pursuant to a Securities Exchange Commission order.

(2) For purposes of subparagraph (1) of this paragraph, it is immaterial whether a deduction has been allowed or an election has been made by the transferor with respect to the specific mineral property transferred.

(3) Where a mineral property is acquired under any circumstance except those described in subparagraph (1) of this paragraph, the taxpayer is not required to take into account the elec-

tion exercised by or deduction allowed to his transferor.

(4) For purposes of applying the limitations imposed by section 615(c): (i) the partner, and not the partnership, shall be considered as the taxpayer (see paragraph (a)(8)(iii) of § 1.702-1), and (ii) an electing small business corporation, as defined in section 1371(b), and not its shareholders, shall be considered as the taxpayer.

(5) For purposes of subparagraph (1)(iii)(b) of this paragraph: (i) if mineral property is acquired from a partnership, the transfer shall be considered as having been made by the individual partners, so that the number of years for which section 615 has been availed of by each partner and the amounts which each partner has deducted or deferred under section 615 shall be taken into account, or (ii) if on interest in a partnership having mineral property is transferred, the transfer shall be considered as a transfer of mineral property by the partner or partners relinquishing an interest, so that the number of years for which section 615 has been availed of by each such partner and the amounts which each such partner has deducted or deferred under section 615 shall be taken into account.

(f) *Examples.* The application of the provisions of this section may be illustrated by the following examples:

Example 1. A calendar year taxpayer who has never claimed the benefits of section 615 received in 1956 a mineral deposit from X Corporation upon a distribution in complete liquidation of the latter under conditions which would make the provisions of section 334(b)(1) applicable in determining the basis of the property in the hands of the taxpayer. During the year 1955 X Corporation expended \$60,000 for exploration expenditures which it elected to treat as deferred expenses. Assume further that the taxpayer made similar expenditures of \$150,000, \$125,000, \$100,000, \$60,000, and \$180,000 for the years 1956, 1957, 1958, 1959, and 1961, respectively, which the taxpayer elected to deduct for each of those years to the extent allowable. No such expenditures were made for 1960. On the basis of these facts, the taxpayer may deduct or defer \$100,000 for each of the years 1956, 1957, and 1958. No deduction or deferral is allowable for 1959 since the 4-year limitation of paragraph (a) of this section applies. The taxpayer may deduct or defer a maximum of \$40,000 for 1961 since the \$400,000 limitation of paragraph (b) of this section applies, but the